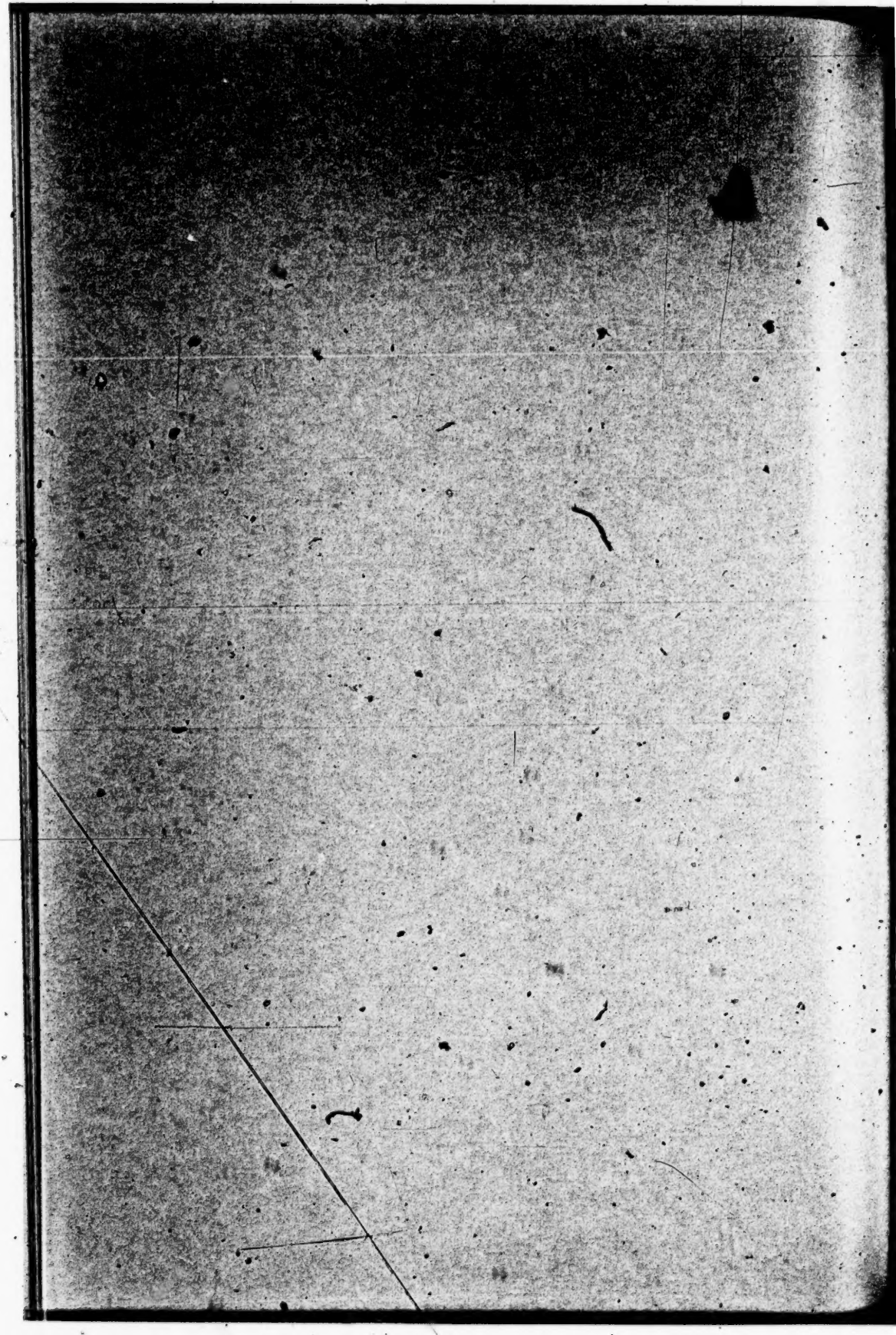


SUBJECT INDEX

	Page
Petition for Writ of Certiorari	1-5
The Question Presented	1-2
Statement	2-3
Reasons Relied on for Allowance of Writ	3-5
Prayer	5
Brief in Support of Petition for Writ	6
I. The Opinions of Courts Below	6
II. Jurisdiction	6
III. Statement of the Case	6
IV. Specifications of Errors	6-7
V. Argument	8-16
Point I. The Circuit Court of Appeals erred in reversing the United States District Court and in denying the petitioner the loss it suffered on its investment in the capital stock of its subsidiaries the Springer and Roy Trading Companies in the sum of $134,792.11	8-11
Point II. The Circuit Court of Appeals for the Tenth Circuit erred in refusing to hold that since Section 2141, Title 26, U.S.C.A. imposed upon corporations making consolidated returns the condition that they consent to all regulations promulgated thereunder by the Treasury Department, that the Treasury Department was not bound by the applicable provisions of Regulations 75 and the express provisions of Regulations 75 require the allowance of the Loss sustained by the petitioner in the year 1929 without reduction on account of Operating Losses sustained by the subsidiaries in years prior to 1929	12-16
CONCLUSION	17
Appendix	18-19-20

TABLE OF CASES CITED

	Page
Burnet v. Imperial Elevator Co., (Not officially reported, but found at p. 2261, Vol. 1, 1933 Prentice-Hall)	4, 10, 11
Commissioner v. Apartment Corp. (Not officially reported, but found at p. 2300.176 Vol. 1, 1933 Prentice-Hall)	4, 11
Delaware & Hudson Co. v. Commissioner, 65 Fed. (2d) 292	10
Hellmich v. Hellman, 276 U. S. p. 233	8
McLaughlin v. Pacific Lumber Co., (Not officially reported, but found at p. 2300.101, Vol. 1, 1933, Prentice-Hall)	4, 11
United Publishers Corp. v. Anderson, 42 Fed. (2d) 781	8, 9
Woolford Realty Co., v. Rose, 286 U. S. p. 319	9, 10

TABLE OF STATUTES AND REGULATIONS CITED

Revenue Act of 1928	
Section 2141, Title 26, U.S.C.A. (Appendix p. 18)	1, 2, 5, 7, 12, 17
Sec. 141 (a)	4, 5, 12
Sec. 141 (b) (Art. 1)	13
Sec. 141 (c)	5, 13
Section 347, Title 28, U.S.C.A.	6
Treasury Regulations 75	
Article 34, subdivision (e) par. 2 (Appendix 19)	7, 15, 16
Article 35	16
Article 37, subdivision (a) (Appendix p. 20)	15
Article 37, subdivision (b) (Appendix p. 19)	15
Article 40, subdivision (c) (Appendix p. 19)	16
Treasury Regulations 78, Sec. 141, Revenue Act 1932	14
Senate Report No. 960, 70th Congress, First Session	13

IN THE

Supreme Court of the United States

OCTOBER TERM, 1933

No. .....

CHARLES ILFELD COMPANY, a Corporation,
PETITIONER

vs.

B. C. HERNANDEZ, Collector of Internal Revenue for the District of New Mexico

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT FOR THE TENTH CIRCUIT
and
BRIEF IN SUPPORT THEREOF.

The Charles Ilfeld Company, a corporation, the petitioner herein, respectfully shows to this Honorable Court, as follows:

THE QUESTION PRESENTED

This case arose in the United States District Court for the District of New Mexico, under the Revenue Act of 1928, effective January 1st, 1929, Section 2141 Title 26, U. S. C. A., and the regulations of the Treasury Department, promulgated by the authority of said Act (See Appendix). The petitioning corporation owned all of the stock of two subsidiaries for ten years during which time consolidated returns were filed. The parent corporation, the petitioner herein, operated at a profit during that period, and the two subsidiaries had a total combined loss of $134,792.11 (See Tr. of Rec. pp. 67, 68).

The subsidiaries liquidated in November, 1929, and the parent petitioner charged off its loss on its investment in the

capital stock of the subsidiaries as of December 31, 1929 (Tr. of Rec. p. 23). The petitioner filed a consolidated return for the year 1929, thereby consenting to be bound by the regulations of the Treasury Department governing consolidated returns, promulgated under the authority granted it under Section 2141 Title 26 U. S. C. A.

The Circuit Court of Appeals for the Tenth Circuit, reversing the trial court, held that the payment of liquidating dividends after affiliation broken, was not an intercompany transaction, but that the commissioner is not forbidden to take into account losses for 1929 and prior years, which were availed of by the petitioning parent corporation during the ten year consolidated return period, by offsetting the operating losses of its subsidiaries in such returns against the operating profits of this petitioning parent corporation. The Circuit Court of Appeals for the 10th Circuit held that the parent corporation, having availed itself of the operating losses in its consolidated returns during the consolidated return period, cannot either under the law existing previous to the revenue Act of 1928, nor under the Regulations thereafter promulgated by authority of the 1928 Revenue Act, Sec. 2141 Title 26, U. S. C. A., deduct the loss on its investment in the capital stock of the subsidiaries for the year 1929. The trial Court held, and this petitioner contends, that it is entitled to deduct such loss on its investment in the capital of the subsidiaries.

STATEMENT

The pertinent facts are as follows:

In 1917, the Petitioner purchased all of the capital stock of the Springer Trading Company and paid therefor, the sum of Forty thousand ($40,000.00) dollars. The Springer Trading Company was operated as an affiliated and going concern until November, 1929. During that period of time, the petitioner advanced to the Springer Trading Company the sum of $69,030.27 and in November, 1929, the Springer Trading Company sold all of its assets to outside interests, paid off all its obligations and ceased to function as a going concern. On December 23, 1929 the Springer Trading Company turned over to the petitioner the sum of $22,914.22, the net cash pro-

ceeds of its liquidation and as of December 31st, 1929, charged off $86,116.05 loss on its investment in the capital stock of the Springer Trading Company. In the taxable years 1918 to 1929, inclusive, the petitioner filed consolidated corporation income tax returns.

The profits of the Springer Trading Company heretofore returned $12,913.88; the aggregate net loss of the parent corporation on its investment in the Springer Trading Company's stock was $86,116.05 (Tr. of Rec. p. 68).

The Roy Trading Company was acquired in 1920, and the facts concerning its operation and liquidation are the same as the Springer Trading Company's.

The petitioner was never permitted, during the consolidated return periods, to charge off its losses on its investment in the stock of its subsidiaries, on its books. (See Exhibits F and H, pages 52 and 53 of the Tr. of Rec.)

The United States District Court for the District of New Mexico found in favor of this petitioner and this petitioner was awarded judgment against the Commissioner in the sum of $14,460.43, on account of overpayment of income taxes for the year of 1929. The Circuit Court of Appeals for the Tenth Circuit reversed the trial court's decision, holding that the operating losses of the subsidiaries having been availed of annually by the parent corporation in yearly returns over the consolidated return period, the parent company after affiliation broken, was not entitled to avail itself of the loss on its capital investment in the capital stock on liquidation, of its subsidiaries.

REASONS RELIED ON FOR ALLOWANCE OF THE WRIT.

1. The Circuit Court of Appeals in holding that the losses of the petitioner on its investment in the capital stock of its subsidiaries charged off from the parent corporation's books as a capital loss as of December 31, 1929, was not a deductible loss against its investment in the capital stock of such subsidiaries, has decided an important question of Federal law which has not been, but should be, decided by this Court.

2. The decision of the Tenth Circuit Court of Appeals herein, is in conflict with decisions of the 8th and 9th Circuit Courts of Appeal. The decision in the instant case is in conflict with the case of *McLaughlin*, Collector, v. *Pacific Lumber Company*, decided September 6, 1933, by the 9th Circuit Court, which is not yet reported in official law reports, but is to be found at p. 2300.101 Prentice-Hall, Vol. 1, 1933, wherein the 9th Circuit Court held such losses deductible. The *McLaughlin* case cannot be distinguished under the facts from the case at bar.

The decision in the instant case is also in conflict with a decision of the 8th Circuit Court of Appeals in the case of *Barnet* v. *Imperial Elevator Company*, decided by the 8th Circuit Court on July 20, 1933 and which is not yet reported, but found in Prentice-Hall, p. 2261, Vol. 1, 1933.

The Circuit Court of Appeals for the Fourth Circuit in the case of *Commissioner* of Internal Revenue v. *Apartment Corporation* in an opinion decided October 3, 1933, followed the decision of the Tenth Circuit Court of Appeals in the instant case, but recognized the conflict between its decision and that of the 9th Circuit Court of Appeals in the case of *McLaughlin* vs. *Pacific Lumber Company*, supra, using the following words:

> "Since the argument of this case, the Circuit Court of Appeals for the 9th Circuit has handed down an opinion dealing with the question involved here—McLaughlin v. Pacific Lumber Company decided September 6, 1933. For reasons given above, we cannot agree with the conclusions there reached."

The Fourth Circuit Court's opinion is not yet reported in an official report, but is found in Prentice-Hall, Vol. 1, 1933, p. 2300.176, paragraph 1800.

3. The question presented is one of great importance because it affects, from a consolidated return income tax point, an interpretation of the power delegated by Congress to make rules governing consolidated returns which will have the force and effect of law. Section 141 (a) of the Revenue Act

of 1928, Sec. 2141 Title 26, U. S. C. A. gives affiliated groups of corporations the privilege of making consolidated returns for the year 1929, and further provides:

> "The making of a consolidated return shall be upon the condition that all the corporations which have been members of the affiliated group at any time during the taxable year for which the return is made consent to all the regulations under subsection (b) *prescribed prior to the making of such return*; and the making of a consolidated return shall be considered as such consent."

Section 141 (c) reads:

> "In any case in which a consolidated return is made the tax *shall be determined*, computed, assessed, collected and adjusted *in accordance with the regulations* under subsection (b) *prescribed prior to the date on which such return is made.*" (Italics ours).

4. The Treasury Department promulgated Regulation 75 under the authority granted it by the terms of Section 2141, Title 26, U. S. C. A. and the applicable provisions of Regulations 75 are binding upon both the government and the taxpayer; and the express provisions of Regulations 75 require the allowance of the loss sustained by the petitioner in the year 1929 without deduction on account of operating losses sustained by the subsidiaries in years prior to 1929.

Wherefore, your Petitioner respectfully prays that a Writ of Certiorari be granted to review the judgment of the United States Circuit Court of Appeals for the 10th Circuit in this case, which is numbered and entitled on its docket: "B. C. Hernandez, Collector of Internal Revenue for the District of New Mexico, Appellant vs. Charles Ilfeld Company, a New Mexico corporation, Appellee, No. 787."

CHARLES ILFELD COMPANY

By A. T. Hannett—P. O. Box 497,
Albuquerque,
Counsel for Petitioner.

BRIEF IN SUPPORT OF PETITION FOR WRIT OF CERTIORARI

I.

THE OPINIONS OF THE COURTS BELOW

The opinion of the United States Circuit Court of Appeals for the Tenth Circuit is reported in 66 Federal (2d) p. 236 (Tr. of Rec. pp. 134 to 144; On Re-hearing pp. 150 to 155).

II.

JURISDICTION

The judgment of the Circuit Court of Appeals was rendered in this case on the 13th day of July, 1933 (Tr. Rec. p. 145). A Petition for Re-hearing was thereafter filed and denied on the 10th day of October, 1933 (Tr. Rec. p. 156). Stay of Mandate was granted by the Circuit Court of Appeals for a period of thirty (30) days from the 19th day of October, 1933, for the petitioner herein to file this Petition with this Court.

The jurisdiction of this Court is invoked under Section 347, Title 28 U. S. C. A.

III.

STATEMENT OF THE CASE

A sufficiently full statement of the case has been given under the heading "Statement" in the Petition for Writ of Certiorari and, therefore, in the interest of brevity, the facts will not be repeated in this brief.

IV.

SPECIFICATIONS OF ERRORS

1. The Circuit Court of Appeals erred in reversing the United States District Court for the District of New Mexico.

2. The Circuit Court of Appeals erred in denying the petitioner the loss which it suffered on its investment in the capital stock of its subsidiaries—the Springer and Roy Trading Companies in the sum of $134,792.11.

3. The Circuit Court of Appeals erred in finding and holding that, irrespective of Treasury Regulations 75 promulgated by the Treasury Department under statutory authority (Section 2141 Title 26, U. S. C. A.) that the petitioner herein was not entitled to a deductible loss on the losses sustained by it on its investment in the capital stock of its subsidiaries.

4. The Circuit Court of Appeals erred in refusing to hold that since the Revenue Act of 1928, Section 2141 Title 26 U. S. C. A. imposed on corporations making consolidated returns, the following:

> "The making of a consolidated return shall be upon the condition that all the corporations which have been members of the affiliated group at any time during the taxable year for which return is made, consent to all the regulations under subsection (b) prescribed prior to the making of such returns; and the making of such a consolidated return shall be considered as such consent."

the Commissioner was not bound to allow the deductible loss here claimed under the provisions of paragraph 2, of subdivision (c) of Article 34, Regulations 75 quoted in Appendix.

5. The Circuit Court of Appeals erred in refusing to hold that both the Government and the petitioner were bound by the applicable provisions of Regulations 75 and that the express provisions of Regulations 75 require the allowance of the loss sustained by the petitioner in the year 1929 without reduction on account of operating losses sustained by the subsidiaries in the years prior to 1929.

V.

ARGUMENT

POINT I.

THE CIRCUIT COURT OF APPEALS ERRED IN REVERSING THE UNITED STATES DISTRICT COURT AND IN DENYING THE PETITIONER THE LOSS IT SUFFERED ON ITS INVESTMENT IN THE CAPITAL STOCK OF ITS SUBSIDIARIES THE SPRINGER AND ROY TRADING COMPANIES IN THE SUM OF $134,792.11.

There is no necessary correlation between the taxation of operating profits, or the deduction of operating losses by a *corporation* and the taxation of gains or the deduction of losses by a *stockholder* from his investment in it. Whether or not the corporation's gains or losses are reflected in the price the stockholder pays or receives for his stock, the income tax law treats the two taxpayers, the corporation and the stockholder, as entirely separate, and taxes their gains independently. Thus X Corporation may have had operating profits of $1,000,000, on all of which it has paid the tax. As a result of these profitable operations, the shares of stock in X owned by A may have advanced from their cost of $100,000 to a market value of $200,000. If X corporation is liquidated and A receives $200,000, as his dividend, A will be compelled to pay an income tax on $100,000 profit, irrespective of the fact that the X corporation has previously paid a tax on these same profits as earned. This Court has held that this double taxation is not invalid, *Hellmich* v. *Hellman* (276 U. S. 233). The converse is also true. As was said in the case of *United Publishers Corporation* v. *Anderson*, reported in 42 Fed. (2d) p. 781:

> "In principle this case cannot be distinguished from Remington Rand, Inc. v. Commissioner of Internal Revenue (C. C. A.) 33 Fed. (2d) 77, certiorari denied in 280 U. S. 591, 50 Sup. Ct. 39, 74 L. Ed. 639. It was there held that where a parent corporation sold its stockholdings in a subsidiary, the excess of the selling price over the cost of the stock was taxable as a profit realized by the parent.

> The fact that the parent had for several years filed consolidated returns was held immaterial, as was also the fact that the subsidiary had accumulated earnings during these years, which earnings had been included in the consolidated earnings and thus taxed. The Government's contention was upheld in both respects. Here we have the exact converse. Here the sale of the stock was at a loss, and the operations of the subsidiary had been conducted at a loss over the years when consolidated returns were filed. The taxpayer is therefore warranted in insisting: first, that upon the sale of the Journal of Commerce stock it suffered a loss of $161,091.85, to the same effect as upon the sale of any other property; and, second, that the fact that the Journal of Commerce Company's operating losses had been taken advantage of by the plaintiff in its payment of taxes on the consolidated basis is of no consequence."

The Tenth Circuit Court of Appeals disposes of this contention, in its original opinion (Tr. of Rec. p. 142) by saying:

> "The plaintiff argues that since in arriving at capital gain, operating profits which have been returned for taxes are not taken into the equation, operating losses which have been allowed as deductions should not be considered. There is some logic and convenience in a clear separation of capital losses from operating losses. There is rough equity in the plaintiff's position that what is sauce for the goose should be sauce for the gander."

It is well established that the provisions authorizing consolidated returns do not change the substantive law to make the affiliated group into a single corporation. They authorize merely a form or method of reporting income. The affiliated corporations remain separate entities, but their respective incomes and deductions are reported on a single return. Thus it has been frequently held that the liability to pay the tax rests upon the several affiliated corporations individually. As the Supreme Court said in *Woolford Realty Co.* v. *Rose* (286 U. S. 319):

> " . . . . The fact is not to be ignored that each of two or more corporations joining (under Sec. 240) in a consolidated return is none the less a taxpayer. Commissioner of Internal Revenue v. Ben Ginsburg Co. (C. C. A. 2d) 54 F. (2d) 238, 239. By the express terms of the statute (Sec. 240 b) the tax when computed is to be assessed, in the absence of agreement to the contrary, upon the respective affiliated corporations 'on the basis of the net income properly assignable to each.' 'The term "taxpayer" means any person subject to a tax, imposed by this Act.' Revenue Act of 1926, Sec. 2a (9) (U. S. C. Title 26, Sec. 1262). A corporation does not cease to be such a person by affiliating with another." (at p. 328).

In the latter case, it was *held* that a parent corporation could *not* deduct on a consolidated return net losses of a subsidiary sustained before affiliation. Even, if the subsidiaries' losses were sustained *during* affiliation, it has been uniformly held, following the *Woolford* case, that the net losses cannot be applied against the income of the parent in a subsequent year. See: *Delaware & Hudson Co. v. Comm'r.* 65 Fed. (2d) 292. The two corporations are regarded as separate entities, and the net loss of the one cannot be carried forward and applied against the income of the other in a later year.

Consequently, when deductions were taken in the consolidated return for the operating losses of two subsidiary corporations, the deductions belonged to those corporations and were taken by them. The parent corporation obtained a benefit from the loss, only by virtue of the statute, whereby the parent was permitted to offset the loss of another taxpayer against its own income. The parent suffered no loss of its own until it liquidated the two subsidiaries in *1929*. In that year, it unquestionably did suffer a loss on its investment in the subsidiaries' stock. The fact that the *subsidiaries* had previously had operating losses or had been permitted by Congress to report them in a consolidated return has no bearing upon the reality or the deductibility of the *parent's* own loss on its investment. This is well brought out in the recent case of *Burnet v. Imperial Elevator Co.*, decided by the Circuit Court of Appeals for the Eighth Circuit on July 20, 1933. In that case, a subsidiary had had operating losses,

which were deducted on consolidated returns for prior years. In 1923, the subsidiary was liquidated, the parent receiving nothing on the liquidation. It, therefore, deducted the full cost of the stock in the subsidiary in that year, and sought to carry it forward as a net loss. The Commissioner urged that the parent was attempting to obtain a double deduction. The Court *held* that the deduction was allowable, saying:

> "Operating losses of the subsidiary are, obviously different from losses on the stock held by the taxpayer, and the Board expressly finds that no deduction was taken for the stock loss in that year."

This case is directly in point here, and the Circuit Court of Appeals for the 9th Circuit in the case of *McLaughlin* vs. *Pacific Lumber Company* decided on September 6, 1933, (not yet reported in an official report, but found at page 2300.101 Prentice-Hall, Vol. 1, 1933) under facts which cannot be distinguished from the facts in the case at bar, held that a similar loss was deductible. The same two questions were raised in *McLaughlin* v. *Pacific Lumber Company*, supra, that were raised in the courts below in this case: that the payment of the liquidating dividends was an inter-company transaction; and if not an inter-company transaction, the losses were fully and effectively recovered by the petitioner for tax purposes by deductions taken in the consolidated returns for previous years. The Circuit Court of Appeals for the 9th Circuit decided both these issues against the government, and in favor of the taxpayer under facts identical with the facts in the case at bar.

The Circuit Court of Appeals for the Fourth Circuit has followed the decision of the Circuit Court of Appeals for the Tenth Circuit in the instant case, in a decision handed down October 3, 1933, in the case of *Commissioner* of Internal Revenue vs. *The Apartment Corporation*, No. 3484 on the docket of the United States Circuit Court of Appeals for the Fourth Circuit. By reason of the conflict of decisions in the four circuits in question, taxpayers in the 8th and 9th Circuits are now permitted to avail themselves of losses similar to the loss here claimed, as deductible, while taxpayers in the 4th and 10th Circuits are denied the right to deduct these losses.

POINT No. II.

THE CIRCUIT COURT OF APPEALS FOR THE TENTH CIRCUIT ERRED IN REFUSING TO HOLD THAT SINCE SECTION 2141 TITLE 26 U. S. C. A. IMPOSED UPON CORPORATIONS MAKING CONSOLIDATED RETURNS THE CONDITION THAT THEY CONSENT TO ALL REGULATIONS PROMULGATED THEREUNDER BY THE TREASURY DEPARTMENT, THAT THE TREASURY DEPARTMENT WAS NOT BOUND BY THE APPLICABLE PROVISIONS OF REGULATIONS 75 AND THE EXPRESS PROVISIONS OF REGULATIONS 75 REQUIRE THE ALLOWANCE OF THE LOSS SUSTAINED BY THE PETITIONER IN THE YEAR 1929 WITHOUT REDUCTION ON ACCOUNT OF OPERATING LOSSES SUSTAINED BY THE SUBSIDIARIES IN YEARS PRIOR TO 1929.

Prior to 1929, regulations promulgated by the Commissioner of Internal Revenue with the approval of the Secretary of the Treasury did not prevent the Government from taking a position contrary to their provisions, as is evidenced by numerous retroactive changes in the regulations, later sustained by the courts. With respect to the regulations promulgated by the Commissioner governing the tax liability of affiliated corporations for the year 1929 and subsequent years, the situation is made entirely different by express statutory provision. Section 141 (a) of the Revenue Act of 1928 —Sec. 2141 Title 26, U.S.C.A. gives affiliated groups of corporations the privilege of making consolidated returns for the year 1929 and further provides:

> "The making of a consolidated return shall be upon the condition that all the corporations which have been members of the affiliated group at any time during the taxable year for which the return is made consent to all the regulations under subsection (b) *prescribed prior to the making of such return;* and the making of a consolidated return shall be considered as such consent." (Italics ours).

This makes the provisions of the regulations binding upon affiliated corporations filing a consolidated return for the year 1929. Likewise, the Government is bound by the provisions of the regulations. Section 141 (c) providing:

> "In any case in which a consolidated return is made the tax *shall be determined*, computed, assessed, collected, and adjusted *in accordance with the regulations* under sub-section (b) *prescribed prior to the date on which such return is made.*" (Italics ours).

It will be observed that in each of the excerpts above quoted it was carefully provided that the regulations in accordance with which the tax must be determined shall have been prescribed prior to the date on which the return is made. For this reason the consolidated returns regulations prescribed by the Commissioner under Section 141 are frequently spoken of as contractual. The bargain cannot be varied by either party.

That this was the object of Congress in enacting Section 141 is shown by the report of the Senate Committee on Finance (Senate Report No. 960, 70th Congress, First Session) at page 15:

> "The committee believes it to be impracticable to attempt by legislation to prescribe the various detailed and complicated rules necessary to meet the many differing and complicated situations. Accordingly, it has found it necessary to delegate power to the commissioner to prescribe regulations *legislative in character* covering them." (Italics ours).

Regulations 75, prescribed by the Commissioner in accordance with the authority granted in Section 141 (b), recognizes the obligation of the Government to be bound by its provisions. Article I (b) provides:

> "The tax liability of the members of the affiliated group for such year will be determined in accordance with such regulations and without regard to any amendment thereto promulgated subsequent to the filing of such return."

The Commissioner thus expressly disclaims the right to make retroactive changes in the consolidated returns regulations for 1929. Nor has he attempted to do so in this case.

The provisions of Regulations 78, prescribed under Section 141 of Revenue Act of 1932, governing consolidated returns for 1932 and subsequent years, so far as they relate to the problem presented in this case, are not different from the corresponding provisions of Regulations 75. Moreover, the Commissioner expressly states in Regulations 78 under the heading "Application of Regulations": "The regulations applicable to the taxable years 1929, 1930 and 1931 will be found in Regulations 75.".

The problem presented by this case is therefore governed solely by the applicable provisions of Regulations 75.

The very first of many difficult and complicated problems arising in the administration of consolidated returns provisions on which the Congress intended to delegate power to the Commissioner to prescribe regulations legislative in character was the problem presented by the instant case. When the Commissioner promulgated Regulations 75 he departed from, we think, an unvarying precedent, and quoted in support of his authority to prescribe regulations the statement made in the report of the Committee on Finance above referred to (noting also a similar statement of the managers on the part of the House), beginning as follows:

> "Among the regulations which it is expected that the commissioner will prescribe are: (1) The extent to which gain or loss shall be recognized upon the sale by a member of the affiliated group of stock issued by any other member of the affiliated group or upon dissolution (whether partial or complete) of a member of the group; * * *".

Carrying out the desire of Congress, thus expressed, that he legislate upon this subject, the Commissioner provided in Regulations 75 the precise method of calculating the taxable gain or deductible loss resulting to a corporation whose subsidiary is dissolved in the taxable year 1929. Article 37 deals with "Dissolutions—Recognition of Gain or Loss." As the opinion of the Circuit Court demonstrates, the transaction out of which the claimed loss arose did not occur during the consolidated return period, the affiliation having been termi-

nated prior to liquidation, and therefore is not to be disregarded as having arisen upon a distribution required under Article 37 (a) to be considered an intercompany transaction. Since the distribution occurred after the consolidated return period, Article 37 (b) is in terms applicable:

> "Any such distribution after a consolidated return period, whether in complete or partial liquidation, shall be treated as a sale of the stock, and the adjustments specified in articles 34 and 35 will be made, and article 36 will be applicable."

Article 36 has no bearing in this case.

The adjustments specified in Article 34 (which affects the determination of the loss on the stock investment of the petitioner, while Article 35 affects the determination of the loss on the inter-company accounts receivable) are contained, so far as applicable to the facts of this case, in paragraph (c) (2). Paragraph (c) prescribes the ordinary basis for determining gain or loss, with a provision for an aggregate basis where several affiliated corporations own the stock of the issuing corporation concerned, and provides for the following adjustment:

> "(2) From the sum of the aggregate bases, as determined in paragraph (1) above, there shall be deducted the aggregate of the losses of such issuing corporation sustained during each of the consolidated return periods (*including only the taxable year 1929 and subsequent taxable years*) after such corporation became a member of the group and prior to the sale of the stock, to the extent that such losses could not have been availed of by such corporation as a net loss in computing its tax for such periods if it had made a separate return for each of such periods." (Italics ours).

It is impossible to spell out more plainly than in the words of this regulation that no part of any losses sustained by the issuing corporation (the liquidated subsidiary) for 1928 or any prior year is to be deducted from the basis for determin-

ing gain or loss on the liquidation. To hold otherwise would be to write the word "only" out of the regulation.

The losses sustained by reason of the non-payment of advances made by the petitioner to the subsidiaries liquidated in 1929 stand on the same footing as the losses sustained upon the stock investment. Article 40 of Regulations 75 entitled "Bad Debts" provides in paragraph (e), "Limitation on Allowance after Consolidated Return Period":

> "The rules applicable to the allowance of losses upon the sale of bonds shall be applicable to the allowance after the consolidated return period as a bad debt of an intercompany account receivable or other obligation resulting from an intercompany transaction during the consolidated return period. (See article 35)."

Article 35, entitled "Sale of Bonds—Basis for determining Gain or Loss," provides for determining the basis of each bond in accordance with the act, adding

> "but the amount of any loss otherwise allowable shall be decreased by the excess (if any) of the aggregate of the deductions *computed under paragraph* (c) (2) of article 34 over the aggregate of the basis of the stock of the issuing corporation as computed under paragraph (c) (1) or (d), as the case be, held by the members of the affiliated group." (Italics ours).

As we have shown above, no deduction is to be made under paragraph (c) (2) of Article 34 from the basis of stock on account of operating losses of the issuing corporations for years prior to 1929, and there is no excess of such deductions available to reduce the basis of bonds, and therefore of these intercompany accounts receivable, under the present circumstances.

It follows that the losses sustained by the petitioner on both the stock and the intercompany accounts receivable are unaffected by operating losses of the subsidiaries unless they occurred in the taxable year 1929.

CONCLUSION

It is therefore respectfully submitted that under the statute and under the Regulations, no other result can be reached than a reversal of the Judgment of the Circuit Court and an affirmance of the decision of the trial court in favor of the taxpayer. It is earnestly represented, moreover, that the Courts should permit no shadow of doubt to fall upon the inviolability of the consolidated returns regulations—contractual in their effect as between government and taxpayer, legislative in their force upon both, and ever since their promulgation, relied upon by affiliated groups of corporations throughout the land as stating the exact tax consequences of transactions which, without such assurances, they might not have undertaken.

Had the petitioner herein filed a separate return for itself and for each of its subsidiaries in 1929, the parent corporation would have been entitled, under any theory of the law or the departmental regulations, to this deduction. Neither the decision in the Fourth, Eighth, or Ninth Circuits involved Section 2141, Title 26, U.S.C.A., or the rules promulgated thereunder, and this case, so far as the petitioner is advised, is the first one ever presented to this Court for an interpretation of the 1928 Act, and the rules promulgated thereunder, touching consolidated returns.

It is therefore respectfully submitted that this case is one calling for the exercise by this Court, of its supervisory powers and that to such an end, the Writ of Certiorari prayed for, should be granted.

Respectfully submitted,

A. T. HANNETT,
P. O. Box 497,
Albuquerque, New Mexico,
Counsel for Petitioner.

APPENDIX

STATUTES AND REGULATIONS REFERRED TO IN PETITION AND BRIEF.

REVENUE ACT OF 1928

Section 2141, Title 26, U. S. C. A.

"Consolidated returns of Corporations—1929 and subsequent taxable years.

(a) Privilege to File Consolidated Returns. An affiliated group of corporations shall, subject to the provisions of this section, have the privilege of making a consolidated return for the taxable year 1929 or any subsequent taxable year, in lieu of separate returns. The making of a consolidated return shall be upon the condition that all the corporations which have been members of the affiliated group at any time during the taxable year for which the return is made, consent to all the regulations under subsection (b) prescribed prior to the making of such return; and the making of a consolidated return shall be considered as such consent. In the case of a corporation which is a member of the affiliated group for a fractional part of the year the consolidated return shall include the income of such corporation for such part of the year as it is a member of the affiliated group.

(b) Regulations. The Commissioner, with the approval of the Secretary, shall prescribe such regulations as he may deem necessary in order that the tax liability of an affiliated group of corporations making a consolidated return and of each corporation in the group, both during and after the period of affiliation, may be determined, computed, assessed, collected, and adjusted in such manner as clearly to reflect the income and to prevent avoidance of tax liability.

(c) Computation and payment of Tax. In any case in which a consolidated return is made the tax shall be determined, computed, assessed, collected, and adjusted in accordance with the regulations under subsection (b) prescribed prior to the date on which such return is made. Only one specific credit, computed as provided in section 2026 (b), shall be allowed in computing the tax."

TREASURY REGULATIONS 75, PROMULGATED BY THE TREASURY DEPARTMENT PURSUANT TO THE AUTHORITY GRANTED BY THE TERMS OF THE ABOVE STATUTE.

SALES WHICH BREAK AFFILIATION MADE WHILE SELLING CORPORATION IS MEMBER OF GROUP:

Paragraph 2, of subdivision (*c*), Article 34:

> "From the sum of the aggregate bases, as determined in paragraph (1) above, there shall be deducted the aggregate of the losses of such issuing corporation sustained during each of the consolidated return periods (*including only the taxable year 1929 and subsequent taxable years*) after such corporation became a member of the group and prior to the sale of the stock *to the extent that such losses could not have been availed of by such corporation as a net loss in computing its tax for such periods if it had made a separate return for each of such periods.*" (Italics ours).

Subdivision (b) of Article 37, Regulations 75, reads:

> "After Consolidated Return Period. Any such distribution after a consolidated return period, whether in complete or partial liquidation, shall be treated as a sale of stock, and the adjustments specified in Articles 34 and 35 will be made, and Article 36 will be applicable."

Subdivision (*c*) of Article 40, Regulations 75, reads:

"Limitation on allowance after Consolidated Return Period.

> The rules applicable to the allowance of losses upon the sale of bonds shall be applicable to the allowance after the consolidated return period as a bad debt of an intercompany account receivable or other obligation resulting from an intercompany transaction during the consolidated return period. (See Article 35)."

Subdivision (a) Article 37, Regulations 75, reads:

> "Gain or loss shall not be recognized upon a distribution during a consolidated return period, by a member of an affiliated group to another member of such group, in cancellation or redemption of all or any portion of its stock; and any such distribution shall be considered an intercompany transaction."